



PUBLIC UTILITIES COMMISSION

STATE OF CALIFORNIA  
505 VAN NESS AVENUE  
SAN FRANCISCO, CALIFORNIA 94102

MICHAEL R. PEEVEY  
PRESIDENT

TEL: (415) 703-3703  
FAX: (415) 703-5091

March 15, 2004

The Honorable Sarah Reyes, Chair  
The Honorable Keith Richman, Vice-Chair  
Assembly Utilities and Commerce Committee  
State Capitol  
Sacramento, CA 95814

Subject: Moving Toward A Workable Electric Retail Market for customers of  
California's Investor-Owned Utilities—A study of the Core/Non-Core Option

Dear Assemblymembers Reyes and Richman:

As you know, I recently had the opportunity to appear before the Assembly Utilities and Commerce Committee to present the 2004 Workplan for the California Public Utilities Commission. A top priority in our Workplan is the production of a credible and detailed study of one approach to balance the desire of electric utility customers for choice as to service offerings and service providers with the needs of the investor-owned electric utilities (IOUs) and the State of California for planning certainty and the timely recovery of costs for generation resources already committed to those customers. I promised to have a study of an electric services market design modeled after the successful core/non-core approach utilized in the natural gas market to this Committee no later than March 15.

I hereby submit the report prepared by our Division of Strategic Planning (DSP) on the important considerations involved in adopting a core/non-core electric market. In doing so, I wish to emphasize that this report has **not** been adopted by the Commission, nor does it reflect my personal preferences on the design of a core/non-core market. Each Commission office has had an opportunity to comment on various drafts, but we have not attempted to conduct hearings, engage in debates, or tried to arrive at a formal consensus on what the Commission recommendations regarding a core/non-core market for electricity ought to be. Rather than delaying the publication of the report for these activities, I thought it more important to place our staff's work in the public domain as the Legislature and Administration consider policy options in this critical issue area.

In transmitting this report to you, I wish to emphasize several areas of disappointment as to the content and completeness of the DSP report.

Commissioner Kennedy and I, who comprise the Commission's subcommittee on legislative matters, requested this report from DSP last year in order to help the Legislature develop an appropriate policy choice for the retail electric market, complete with an implementation schedule and commitment by the Commission to resolve critical cost, supply, rate, and other threshold issues. We envisioned the study as developing a clear set of guideposts for resolving differences in competing legislative proposals. And, in the absence of new legislation to replace the current patchwork of post-AB 1890 statutory directives and prohibitions, the study would serve as the Commission's preferred policy choice, subject to endorsement or revision by the Legislature and Governor. Unfortunately, I think the DSP study has limited value for these purposes, because while it does contain useful analytical principles and notes areas of general concern, such as assuring adequate energy supplies and avoiding cost shifting between core and non-core customers, it does not endorse a core/non-core approach because of general concerns stated in the body of the study. Consequently, it is seriously deficient in presenting a fleshed-out core/non-core proposal with sufficient detail for full evaluation by all interested parties.

In contrast to the staff view, I do support a core/non-core reform for reasons the report fails to adequately embrace, including the value to large customers of gaining increased control over the costs and terms of delivery of their electricity by choosing among suppliers, and the presence of competing suppliers to cause utilities to be more efficient in acquiring and delivering energy supplies, which redounds to the benefit of both core and non-core customers. In addition, I believe there are many benefits beyond cost savings to customers when we increase competition in the retail electric market, such as innovation, as well as basic improvements in customer service. While I fully acknowledge the reality of paying off the DWR contracts and assuring both utilities and customers of a stable and adequate supply options, the DSP report seems overly timid in creating a vision of what is possible. Specifically, I believe that (1) large customers with loads smaller than 500kw should be allowed to depart the utility system under rules fair to the utility and core customers (2) the number of large customer participants should not be as limited as the DSP study recommends (3) aggregation of all size loads should be allowed, beyond that mandated in the recent community aggregation legislation, and (4) the program should be put in to place much earlier than the 2009 start date. Let me reassure you that the introduction of the core/non-core reform will be incremental, with careful monitoring to avoid the negative consequences raised in the study.

If there is one overriding principle that all parties to this debate can agree on, it is this—uncertainty in what California's retail market rules are or will be is very undesirable economically. Utilities cannot make plans. Non-utility energy suppliers cannot make plans, nor will they make capital commitments. Utility customers, including those who will play a vital role in rebuilding California's struggling economy, will be denied choice and the opportunity to fully control an often critical cost center. Wall Street analysts will continue to note California's "uncertain regulatory environment". Therefore, while I submit the DSP report on a timely basis, I further commit to move this topic to consideration by our full Commission on an expedited basis. I intend to sponsor a core/non-core proposal that corrects the shortcomings I see in the DSP report. My version will provide choice for the non-core, as well as choices for core customers, including time of use rates, real time pricing, and green pricing options. I will invite public comment on the proposal and then place it on the Commission's public agenda. As with the Energy Action Plan, I intend to fully cooperate with the Energy Commission and other state energy agencies in developing what I hope will become a Commission initiative.

In the meantime, I pledge the full cooperation of the Commission and its staff to assist you and other members of the Legislature and the Administration in assessing the current legislative proposals to adopt a post-crisis retail marketplace.

Very truly yours,



MICHAEL R. PEEVEY  
President

C: Hon. John Burton, President Pro Tempore of the Senate  
Hon. Fabian Nunez, Speaker of the Assembly  
Hon. James L. Brulte, Senate Republican Leader  
Hon. Kevin McCarthy, Assembly Republican Leader  
Hon. Debra Bowen, Chair, Senate Energy Utilities & Communications Committee  
Hon. Bill Morrow, Vice-Chair, Senate Energy, Utilities & Communications Committee  
Members, Senate Energy Utilities & Communications Committee  
Members, Assembly Utilities & Commerce Committee  
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